82-1516

No. _____

IN THE

SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1982

SEA PINES COMPANY,

Petitioner

v.

FEDERAL DEPOSIT INSURANCE CORPORATION,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

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Dated: March 4, 1983

Questions Presented

1. Whether the corporate veil of a parent corporation should be pierced to protect a creditor of a subsidiary corporation by looking at only two isolated transactions between the parent and the subsidiary rather than all of the transactions between the two entities.

2. Whether a parent corporation has committed an "injustice or fundamental unfairness" toward its subsidiary's creditors by taking $350,000.00 out of the subsidiary when the parent and another subsidiary had put into the subsidiary in excess of $3,500,000.00 to use in paying its creditors, employees and other expenses.

3. Whether one of many creditors of a subsidiary corporation is entitled to full recovery of assets that a court had found were wrongfully removed by the parent corporation rather than a pro rata share of such assets.

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Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

The Petitioner, Sea Pines Company[1], respectfully prays that a Writ of Certiorari be issued to review the Judgment of the United States Court of Appeals for the Fourth Circuit in this case.

Opinions Below

The opinion of the Fourth Circuit (App. *infra*, pp. 1a-12a) has not yet been officially reported. The opinion of the district court (App. C *infra*, p. 14a) is not reported.

[1]Sea Pines Company has partial ownership in the following subsidiary companies: Point South, Inc.; Sea Pines Behavioral Institute, Inc.; Sea Pines Land Company, Inc.; and Hilton Head Ocean Front Rentals, Inc.

Jurisdiction

The judgment of the Court of Appeals (App. A, 1a) was entered on October 28, 1982. A Petition for Rehearing was denied on December 8, 1982 (App. B, *infra*, 13a). The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

Statement

This case originated when the Respondent, Federal Deposit Insurance Corporation (FDIC), a United States Agency, acquired from the receiver of a failed banking institution, American Bank & Trust (AB&T), a Two Hundred Fifty Thousand ($250,000.00) Dollar note and mortgage dated April 13, 1973, made by Point South, Inc. (Point South). FDIC subsequently foreclosed the mortgage and, on May 28, 1978, obtained a deficiency judgment against Point South in the amount of One Hundred Ninety Six Thousand Six Hundred Eighty and 08/100 ($196,680.08) Dollars. Point South was, at the date of the note and mortgage and at the time of this action, a subsidiary corporation of the Petitioner, Sea Pines Company (Sea Pines), Sea Pines owning ninety (90%) percent of the capital stock of Point South.

On October 16, 1978, FDIC brought this action against Sea Pines to collect the indebtedness owed by Point South. After receiving evidence from both parties, the District Court made findings of fact and held that FDIC could not collect its judgment against Point South from Sea Pines, its parent corporation (p. 29a). The Court concluded that Sea Pines had not guaranteed the debt of Point South to AB&T and that the corporate veil of Point South could not be pierced since FDIC had failed to prove the necessary element of "injustice or fundamental un-

fairness" (p. 29a). The Court of Appeals reversed and held that the corporate veil of Point South should be pierced in that the actions of Point South and Sea Pines were fundamentally unfair to AB&T, FDIC's predecessor in interest (p. 12a). A Petition for Rehearing was denied by the same three-judge panel (p. 13a).

Reasons for Granting the Writ

The decision of the United States Court of Appeals for the Fourth Circuit completely overlooks and ignores the facts before the Court in the present litigation and conflicts with the settled law of the Fourth Circuit and elsewhere setting forth the standard to be followed in an action to pierce the corporate veil. In particular, the decision overlooks the early decision in the Fourth Circuit of *DeWitt Truck Brokers, Inc. v. W. Ray Flemming Fruit Company,* 549 F. 2d 681 (4th Cir. 1976).

The federal courts have consistently held, in accordance with *DeWitt,* that the separate entity of a corporation will ordinarily be recognized and upheld and that the corporate entity will be disregarded only under exceptional circumstances, as where a corporation is a mere shell serving no legitimate business purpose and is used principally as an intermediary to perpetrate fraud or promote injustice. *Chengelis v. Cenco Instruments Corp.,* 386 F. Supp. 862 (D.C. Pa. 1975), affirmed 523 F. 2d 1050 (3rd Cir. 1975); *U.S. v. Martin,* 337 F. 2d 171 (8th Cir. 1964); *In re Gibraltor Amusements Ltd.* 291 F. 2d 22 (2nd Cir. 1961); *Farmers Feed and Supply Co. v. U.S.,* 267 F. Supp. 72 (D.C. Iowa 1967). The Petitioner particularly calls the attention of the Court to the 3rd Circuit case of *Chengelis,* where the Court held that a party who knowingly limits its contractual relationship to one of two related corporate

enterprises cannot successfully attack the validity of the entity with which it dealt without proof of misrepresentation or other unusual circumstances justifying the appliance of an estoppel.

The Court overlooked the existing relationship between the Defendant and Point South, Inc. The Defendant, Sea Pines Company, owned ninety (90%) percent of the corporate stock of Point South, Inc. Over a period of years, commencing about 1965 and continuing until 1979, Sea Pines Company and its fully owned subsidiary, Sea Pines Plantation Company, had advanced to Point South, Inc., approximately $4,000,000.00, which was used by Point South, Inc., to pay its creditors and employees. From the time of the transactions upon which the Circuit Court based its decision until Point South, Inc., discontinued operations, Sea Pines Company and Sea Pines Plantation Company advanced over an additional $2,000,000.00 to Point South, Inc. (At the time of the transactions complained of, Sea Pines Company and Sea Pines Plantation Company had advanced approximately $1,600,000.00).

The Court based its decision basically on a lease-back transaction which Point South, Inc., had entered into and on the mortgage of property of Point South, Inc., from which Sea Pines Company received $350,000.00. In 1974, at a time when advances to Point South, Inc., were approximately $2,000,000.00, Sea Pines Company borrowed $350,000.00 on property of Point South, Inc., which had a value of $350,000.00. This money was used by Sea Pines Company for the benefit of itself and its subsidiaries. Point South, Inc., benefitted tremendously since it received, between 1974 and 1979, approximately $2,000,000.00 from Sea Pines Company and Sea Pines Plantation Company, or far more than $350,000.00.

Without the mortgage transaction in October, 1974, Sea Pines Company may have been forced out of business, and the result of same was to keep Point South, Inc., in business with new cash flowing into Point South, Inc., from Sea Pines Company and Sea Pines Plantation Company. The second transaction was the cancellation of a lease under which Sea Pines Company had guaranteed certain rental to Point South, Inc. The cancellation did benefit Sea Pines Company by allowing it to remain solvent in the years when it had substantial financial problems. The loss to Point South, Inc., was not shown by Plaintiff, but it would have been a small percentage of the $4,000,000.00 due Sea Pines Company and Sea Pines Plantation Company.

The Court erred in the following particulars:

(a) It failed to consider the entire history of the relationship of Point South, Inc., to Sea Pines Company, beginning in 1965 and continuing at least until 1979. If it had so considered the history, it would have found that there was no element of injustice or fundamental unfairness as required by *DeWitt Truck Brokers, Inc. v. W. Ray Flemming Fruit Company, supra.* In fact, any injustice or fundamental unfairness would have been towards Sea Pines Company, not to Point South, Inc.

(b) The Court failed to consider and give any weight to the fact that if the interests of creditors such as Plaintiff were in fact affected adversely, then the Plaintiff still would be limited to a pro-rata recovery of any assets that the Court might find were received from the possession of Point South, Inc. If Sea Pines Company and Sea Pines Plantation Company had paid, through loans to Point South, Inc., all creditors other than the American Bank and Trust Company (FDIC), then they too, became creditors and should have participated in any assets

deemed improperly used by Sea Pines Company in a pro-rata fashion.

The Court of Appeals has decided that FDIC, an unsecured creditor, will recover one hundred (100%) percent of its losses while other *bona fide* creditors such as Sea Pines Company and Sea Pines Plantation Company are not allowed to recover their losses from these new assets.

The *DeWitt* case, in line with the general rule across the country, requires proof of injustice or fundamental unfairness. The overall relationship between Sea Pines Company and Point South, Inc., including the advance of large sums of money by the former to the latter indicate that, contrary to there being any injustice or fundamental unfairness to Point South, Inc., or its creditors, the actual injustice or fundamental unfairness was to the stockholders of Sea Pines Company. Unlike the conventional case in which an attempt is made to pierce the corporate veil (such as *DeWitt*), this case involved money moving in large amounts from the parent corporation to the subsidiary, which money was used by the subsidiary to pay its operating expenses and creditors. Thus, the Court of Appeals failed to look at the total relationship between Sea Pines Company and Point South, Inc. If it had reviewed the transactions between Sea Pines Company and Point South, Inc., it could not have found the necessary element to pierce the corporate veil — injustice or fundamental unfairness.

Conclusion

The Court of Appeals departed from the rule set forth in *DeWitt* which states the general law in the nation. A substantial injustice has been done to the Defendant on facts which demanded a different result. The decision of the Court of Appeals is clearly erroneous and the Court failed to consider the numerous transactions between the parties and only considered transactions where the money involved was a small portion of the moneys due Sea Pines Company by Point South, Inc.

Therefore, the Petition for a Writ of Certiorari should be granted.

Respectfully submitted,

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Dated:

Appendix A
Opinion of United States Court of Appeals

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 81-2134

FEDERAL DEPOSIT INSURANCE CORP.,
Appellant,

v.

SEA PINES COMPANY,
Appellee.

Appeal from the United States District Court for the District of South Carolina at Charleston.
C. Weston Houck, *District Judge.*

Argued: May 4, 1982 Decided: October 28, 1982

Before HALL and SPROUSE, *Circuit Judges,* and DOUMAR*, *District Judge*

J. Randolph Pelzer, Pelzer and Chard, P.C., Office of General Counsel, Federal Deposit Insurance Corp., for Appellant; H. Brewton Hagood, Morris D. Rosen, Barry L. Johnson, Joab M. Dowling, for Appellee.

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*Honorable Robert G. Doumar, United States District Judge for the Eastern District of Virginia, sitting by designation.

Appendix A

Opinion of United States Court of Appeals

DOUMAR, *District Judge:*

This matter is on appeal from the decision of the District Court for the District of South Carolina, wherein the plaintiff/appellant, the Federal Deposit Insurance Corporation (FDIC) alleged that Sea Pines Company, the parent, guaranteed a particular indebtedness of its subsidiary, Point South, Inc., to the American Bank & Trust Company (AB&T), the predecessor in interest to FDIC. Alternatively, FDIC sought to pierce the corporate veil of Point South, Inc. The Court held that Sea Pines Company, the parent, did not guarantee the particular indebtedness. The District Court also concluded that the actions of the parent through the subsidiary were neither unjust nor fundamentally unfair and therefore declined to pierce the corporate veil. We reverse and remand.

Point South, Inc. was one of a number of subsidiary corporations utilized by the parent, Sea Pines Company. Point South, Inc. was initially capitalized with $1,000 by Charles B. Frazier and Joseph B. Frazier, Jr., who were two of the three-man executive committee of Sea Pines Company, the parent.[1] The subsidiary issued one hundred shares of capital stock and later 10% of its stock was transferred to Continental Mortgage Investors, and the remaining 90% of the stock was ultimately assigned to Sea Pines Company.

On February 19, 1973 AB&T issued to the subsidiary a loan commitment for $250,000 for a construction loan mortgage to enable Point South, Inc. to build a reception center on a parcel of the subsidiary's property, near the intersection of U.S. Highway 17 and Interstate 95 in South

[1] See R-1183; See R-683 through 702. They became members of the board of directors of Point South, Inc.

Carolina, to attract potential buyers to a planned development. The commitment itself was not assignable. The loan was closed on or about April 13, 1973, but the project was not funded at once as it was a construction loan. By September 4, 1973, approximately $133,000 of the $250,000 of the construction loan had been disbursed to Point South, Inc. There was no prohibition against assignability in the final note or mortgage, nor did the instrument call for an acceleration of the due date of the principal amount upon the sale of the property.

In August, 1973, Point South, Inc., the subsidiary, desired to sell the property to Point South Associates, a limited partnership, and lease it back. On August 29, 1973, Jeffrey Rhodes, then the assistant to the president of Sea Pines Company, wrote AB&T a letter on Sea Pines stationery which provided in pertinent part as follows:

> Pursuant to our phone conversation, enclosed please find the documents for the sale/leaseback of the Point South Reception Center.
>
> As we discussed Point South intends to sell the building and assign the mortgage to the purchasing entity. Point South Company and Sea Pines Company will guarantee the financing.
>
> We have preserved your first right of refusal to provide the permanent financing.

AB&T did not respond to Mr. Rhodes' letter. The rent payable by Point South, Inc., the subsidiary, to Point South Associates (a/k/a Point South Company), the limited partnership, was guaranteed by Sea Pines Company, by a formal guarantee duly acted upon by the parent (R-742). However, no formal guarantee of the construction loan mortgage was ever issued to or requested by

AB&T. The transaction was finalized on September 7, 1973.

In October, 1974, the subsidiary, Point South, Inc., and Sea Pines Company, acting through the common directors, mortgaged the equity of Point South, Inc. in a 76-acre tract as collateral for the loans of Sea Pines Company, the parent. The parent credited the debts which the subsidiary owed to the parent as alleged consideration for the subsidiary mortgaging its property and allowing the proceeds to go to the parent.

On May 30, 1975, the common directors of the corporations caused the sale and leaseback between Point South, Inc. and Point South Company to be canceled and Point South, Inc. repurchased the property. Point South, Inc. canceled the note and mortgage owed to it by Point South Associates, which was originally in the sum of $55,000. Sea Pines Company was released from its guarantee of rent payments on the reception center.

In February, 1973, Point South, Inc., the subsidiary, had a balance sheet showing properties or assets in excess of $2.5 million with a total net worth of $65,000, of which $1,000 was capital stock and $64,000 was retained earnings.[2] This highly leveraged subsidiary lost $242,000 between February, 1973 and February, 1974. In February, 1974, Point South, Inc. was insolvent, with a negative net worth of $177,000.[3] From February, 1974 until February,

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[2] The record indicates that the consolidated financial statements of February, 1973, after auditing, showed $65,000 net worth (R-475), although the balance sheet forwarded to AB&T unaudited indicated a net worth of $108,082 (R-752). Obviously, this audit reduced the figures.

[3] R-480.

1975, Point South, Inc., the subsidiary, continued to lose money so that by February, 1975, the total insolvency or negative net worth of Point South, Inc. was $1,949,000.00[4].

The District Court concluded that Sea Pines Company did not guarantee the indebtedness of Point South, Inc. and refused to pierce the corporate veil of Point South, Inc. finding no fundamental unfairness. On appeal, FDIC contends that the District Court erred in finding that the letter, from Jeffrey Rhodes dated August 29, 1973, did not guarantee the "indebtedness" of Point South, Inc. to AB&T and that the actions of the common directors of Point South, Inc. and Sea Pines Company were not fundamentally unfair.

I.

The initial contention of the plaintiff is that the letter of August 29, 1973 by Jeffrey Rhodes, constituted a valid guarantee by Sea Pines to AB&T for the construction loan mortgage on the reception center.

The parent maintains that there was no consideration for or acceptance of the guarantee by AB&T, that there was no showing that Jeffrey Rhodes had any authority to make such a guarantee, and finally, that there was no indication that what was written was in any way a guarantee. The parent maintains that the word "guarantee" in relation to Point South Company (Associates) and Sea Pines Company, refers to the sale and leaseback of the reception center. Additionally, the parent contends that the word "financing" was a reference to the agreement of the parent to guarantee the rent due by the subsidiary, under

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[4] R-484.

the lease of the reception center, to the purchaser, Point South Company (Associates), the limited partnership.

FDIC contends that the initial commitment prohibited assignment of the mortgage and that this letter was forwarded to AB&T to receive their consent to the assignment of the mortgage. This, they contend, enabled the purchaser, P oint South Company, to continue to receive the funds or proceeds of the construction mortgage loan of which approximately 50% was still unfunded as of September 1, 1973. FDIC further argues that the word "guarantee" could not refer to the guarantee of the lease payments or financing inasmuch as Point South Company (Associates) would not be guaranteeing the lease payments or rent to itself.

The District Court found that the plaintiff failed to show: consideration for the alleged guarantee; and that there was an acceptance of the alleged guarantee by AB&T as required by South Carolina law. The District Court concluded that the plaintiff failed to meet its burden of proving the essential elements of the alleged guarantee.

For the reasons hereinafter set forth, it is unnecessary for us to decide whether the letter did or did not constitute a valid accepted guarantee.

II.

The appellant argues that the District Court's finding that actions of Point South, Inc. did not fit into a pattern of fundamental unfairness or injustice is clearly erroneous, and, therefore, the corporate veil should be pierced. FDIC contends that Sea Pines Company dominated Point South, Inc. and used the subsidiary for its benefit and to the detriment of the creditors of Point South, Inc. The appellee, Sea Pines Company, contends

that FDIC failed to firmly establish sufficient grounds for the Court to find that the subsidiary was the alter ego of the parent and to establish that there was an injustice committed or fundamental unfairness exhibited sufficient for the piercing of the corporate veil. They urge this Court to adopt a stringent view of injustice amounting to a fraud.

It would serve no useful purpose to reiterate the postulates set forth by this Court in the case of *DeWitt Truck Brokers v. W. Ray Flemming Fruit Co.*, 540 F.2d 681 (4th Cir. 1976), since the District Court found that a sufficient number of the factors to pierce the corporate veil were present except the existence of injustice or fundamental unfairness.

The District Court found as a fact, *inter alia*, the following:

(1) Point South, Inc. was a subsidiary corporation of Sea Pines Company. Sea Pines Company owns 90% of Point South, Inc.

(2) Point South, Inc. is a South Carolina corporation.

(3) Sea Pines Company is a Georgia corporation principally operating in South Carolina.

(4)Point South, Inc. and Sea Pines Company had common directors and officers.

(5)Point South, Inc. adhered to corporate formalities.

(6)Point South, Inc. was financed in large part by Sea Pines Company.

(7) Sea Pines Company paid the salaries and expenses of Point South, Inc. with the expectation that they would be reimbursed.

(8) Sea Pines Company caused the property

owned by Point South, Inc. to be mortgaged for the benefit of Sea Pines Company.

(9) During the period in question, the executives and officers of Point South, Inc. did not act independently of those of Sea Pines Company.

(10) AB&T made a loan to Point South, Inc. for the construction of a reception center. Point South, Inc. sold the property to Point South Company, a limited partnership, and leased it back. The payments on the lease were guaranteed by Sea Pines Company.

(11) AB&T continued to advance money for the reception center to Point South, Inc. until 1974 when the advances were made directly to Point South Company for interest only.

The District Court refused, however, to hold the parent stockholder liable for the debts of Point South, Inc. to AB&T. The Court's rationale centered upon the knowledge that AB&T had or should have had concerning the control which the parent exerted over the subsidiary. The District Court found that AB&T knew or reasonably should have known of the stock ownership of the subsidiary, as well as the common board of directors. In addition, the Court held that the Bank should have known that the subsidiary was undercapitalized and essentially the alter ego of Sea Pines at the time it made the initial loan to Point South, Inc. The District Court concluded that there was no deceit or fraud by either Point South, Inc. or Sea Pines Company and, therefore, there was no fundamental unfairness or injustice.

We reverse the Court inasmuch as we find that the actions of Point South, Inc. and Sea Pines Company were

fundamentally unfair to AB&T, a creditor of Point South, Inc. and predecessor in interest to the plaintiff/appellant, FDIC.

The District Court misconstrued this Court's decision in *DeWitt, supra.* In that case, this Court found fundamental unfairness as a predicate to piercing the corporate veil; however, fundamental unfairness did not necessarily require the existence of fraud and deceit. *Id.* Thus, in the absence of fraud and deceit, injustice or fundamental unfairness can exist, and where they so exist courts have reluctantly and cautiously pierced the corporation's protective veil. *DeWitt, supra. See also Anderson v. Abbott,* 321 U.S. 349 (1944); *Krivo Industrial Supply Co. v. National Distill. & Chemical Corp.,* 483 F.2d 1098 (5th Cir. 1973); *Duplane Corp. v. Deering Milliken, Inc.,* 444 F.Supp. 648 (D. S.C. 1977).

In order to understand the basis for such, we must delineate the duties of directors. In *Koehler v. Black River Falls Iron Co.,* 90 U.S. (2 Black) 715, 720 (1862), the Court said that directors "hold a place of trust and by accepting the trust are obliged to execute it with fidelity, not for their own benefit, but for the common benefit of the stockholders of the corporation." Further, the Supreme Court has stated that "(t)he relation of the directors to corporations is of such a fiduciary nature that transactions between boards having common members are regarded as jealously by the law as are personal dealings between a director and his corporation..." and that those transactions must be shown to be fair in order to maintain the transaction. *Geddes v. Anaconda Copper Mining Co.,* 254 U.S. 590, 599 (1921).

However, when the corporation becomes insolvent,

the fiduciary duty of the directors shifts from the stockholders to the creditors.

> The law by the great weight of authority seems to be settled that when a corporation becomes insolvent, or in a failing condition, the officers and directors no longer represent the stockholders, but by the fact of insolvency, become trustees for the creditors, and that they then cannot by transfer of its property or payment of cash, prefer themselves or other creditors...*Davis v. Woolf,* 147 F.2d 629, 633 (4th Cir. 1945). *See also Alexander, et al v. Hillman,* 296 U.S. 222 (1935).

In this case, the common directors had to have known by February, 1974, that Point South, Inc. was insolvent.[5] On October 6, 1974, while Point South was insolvent, its directors mortgaged the only unencumbered piece of property owned by the subsidiary (which was worth $350,000) for the debts of the parent. Sea Pines Company indicated that it credited the subsidiary's account $8,000 in consideration for the mortgage. In essence, the subsidiary mortgaged its property to secure and to pay for the loans of the parent. This was in no way beneficial to the subsidiary.

It is difficult to materially distinguish this incident from the decision of *Koehler v. Black River Falls Iron Co., supra.* There, the corporate officers placed a mortgage on the property of the corporation at a time when it was insolvent in order to secure the debts owed to themselves. The Court held as follows, *supra,* at 720:

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[5] See discussion on finances, *supra.* The corporation was insolvent in February, 1974, and between February, 1974 and February, 1975, on an average, Point South, Inc. was losing in excess of $30,000 per week.

> Instead of honestly endeavoring to effect a loan of money, advantageously, for the benefit of the corporation, these directors, in violation of their duty, and in betrayal of their trust, secured their own debts, to the injury of the stockholders and creditors. Directors cannot thus deal with the important interests entrusted to their management.

Here, the common directors were violating their duty by securing the debts of their only viable master, the parent, to the detriment of the creditor, plaintiff herein.

This is not the sole transaction with which we are concerned which was fundamentally unfair and unjust. In May, 1975, when Point South, Inc. was virtually $2 million in debt and insolvent, the board of directors of the subsidiary caused the sale and leaseback to be canceled. Point South, Inc. repurchased the property and canceled the $55,000 note due to the subsidiary by the partnership. This transaction also canceled the guarantee by the parent to the partnership of the subsidiary's rent.

At oral argument, counsel for Sea Pines Company was asked for whose benefit did the cancellation of the sale and leaseback and the repurchase of the property occur. Counsel admitted there was no benefit to the insolvent subsidiary but rather the cancellation and repurchase was for the sole benefit of the parent.

Each of these transactions clearly shows that the board of directors of the insolvent corporation was using that corporation and its assets for the benefit of the parent, Sea Pines Company, and not for the subsidiary. The parent, through the interlocking boards of directors, manipulated the assets, property and liabilities of the subsidiary. The directors violated the fiduciary duty owed to the creditors of the insolvent Point South, Inc. These two

transactions clearly indicate fundamental unfairness and injustice.

The District Court had concluded that AB&T knew of the common directorships and should have known of the undercapitalization at the time it made the loan[6]. We feel that there was no evidence to indicate that AB&T knew or should have known that the directors would breach their fiduciary duties by stripping the subsidiary of its assets, when it became insolvent, for the benefit of the parent. It is these unjust and fundamentally unfair acts, not just the interlocking directorships and undercapitalization which causes us to set aside the corporate cloak. *DeWitt, supra; Cf., Bernardin, Inc. v. Midland Oil Corp.*, 520 F.2d 771 (7th Cir. 1975) (absence of fraud and deceit where the parent unjustly stripped the insolvent subsidiary of its assets). We find that the acts of Point South, Inc. and Sea Pines Company mentioned herein were fundamentally unfair and the determination of the District Court to the contrary is REVERSED.

The decision of the District Court is REVERSED AND REMANDED in order that the District Court may enter judgment for the plaintiff against Sea Pines Company for the deficiency, interest and costs, and determine if the plaintiff is or should be entitled to attorney's fees.

REVERSED AND REMANDED.

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[6] *But see* Footnote 2 where AB&T was led to believe that the subsidiary had a net worth of $108,082 at the time the loan was made.

Appendix B
Order of the United States Court of Appeals or Petition for Rehearing

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 81-2134

Federal Deposit Insurance Corporation,
Appellant,

versus

Sea Pines Company,
Appellee.

ORDER

Upon consideration of the appellee's petition for rehearing and suggestion for rehearing en banc, and no judge having requested a poll on the suggestion for rehearing en banc,

It is ADJUDGED and ORDERED that the petition for rehearing is denied.

Entered at the direction of Judge Doumar, U.S.D.J., with the concurrence of Judge Hall and Judge Sprouse.

For the Court,

/s/ William K. Slate, II

Clerk

Appendix C
Oral Order of United States District Court

IN THE UNITED STATES DISTRICT COURT
DISTRICT OF SOUTH CAROLINA
CHARLESTON DIVISION

FEDERAL DEPOSIT INSURANCE CORPORATION,	)	
Plaintiff,	)	CIVIL ACTION
VS.	)	NO. 78-1838-2
SEA PINES COMPANY,	)	
Defendant.	)	
	)	

United States Courthouse,
Charleston, South Carolina
Monday, 2:30 P.M.,
September, 21, 1981

ORAL ORDER OF THE COURT

Appearances:

J. RANDOLPH PELZER, ESQ.,
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MORRIS D. ROSEN, ESQ.,
AND
JOAB M. DOWLING, JR., ESQ.
Beaufort, South Carolina
Attorneys for the Defendant.

Appendix C

Oral Order of United States District Court

THE COURT:

The plaintiff in this case, the Federal Deposit Insurance Corporation, is the successor-in-interest to American Bank and Trust Company. American Bank and Trust Company, on or about April 13, 1973, loaned approximately $250,000 to a South Carolina corporation known as Point South, Inc. For this loan, American Bank and Trust Company received a note, evidencing the loan, and a mortgage on certain property securing that loan. These documents were duly recorded in the Office of the Clerk of Court for Jasper County, South Carolina. The property forming security of the loan will be referred to as the reception center site, being a portion of the property being developed by Point South, Inc., in South Carolina, at the intersection of U.S. Highway 17 and Interstate 95. Point South, Inc., is a subsidiary corporation to the defendant Sea Pines Company, the defendant Sea Pines Company owning approximately ninety percent of the stock in Point South, Inc., at all times herein involved. After making the loan to Point South, Inc., the plaintiff, or the plaintiff's successor — excuse me — or the plaintiff's predecessor-in-interest here, American Bank and Trust Company, was required to foreclose the mortgage because of the failure of Point South, Inc., to make payments thereunder. The plaintiff or its predecessor-in-interest, American Bank and Trust Company, obtained a deficiency judgment as a result of that foreclosure proceeding, and this suit is brought against the defendant, Sea Pines Company, to collect that deficiency judgment.

The complaint contains two general theories of law. One is that the defendant, Sea Pines Company, is liable because it guaranteed the aforementioned obligation of

Point South, Inc., to American Bank and Trust Company. The second theory of liability is that Point South, Inc., was the alter ego of Sea Pines, Inc., and through the theory of piercing the corporate veil, the defendant, Sea Pines Company, should therefore be responsible for the deficiency obtained against Point South, Inc., as a result of the indebtedness in question.

We have tried this case. We have heard the testimony, we have received memoranda, argument, briefs of the attorneys, and now, pursuant to Rule 52 of the Federal Rules of Civil Procedure, we publish the following findings of fact and conclusions of law.

Findings of fact:

1. The plaintiff, Federal Deposit Insurance Corporation, is an agency of the United States of America, and is organized and exists under the laws of the United States.

2. The defendant, Sea Pines Company, is a Georgia corporation doing business at Hilton Head Island, South Carolina, and elsewhere in the State of South Carolina and the United States, but the principle place of business is at Hilton Head Island, South Carolina.

3. The Federal Deposit Insurance Corporation is the successor-in-interest to the American Bank and Trust Company.

4. On or about February 9, 1973, David G. Gale, assistant vice-president of American Bank and Trust Company wrote a letter to Point South, Inc., setting forth the terms and conditions of an offer for a non-assignable loan commitment for the construction and development by Point South, Inc., of property known as the reception center site located at Point South, Jasper County, South Carolina, at the intersection of U.S. Highway 17 and I-95.

5. On or about February 15, 1973, James F. Russell, group financial manager of Sea Pines Corporation and its subsidiaries including Point South, Inc., wrote a letter to Mr. Gale accepting the loan commitment as set forth in the February 9, 1973, letter on behalf of Point South, Inc., subject to the agreement of American Bank and Trust Company of several amendments and/or additions to the terms and conditions of the proposed loan.

6. On or about April 13, 1973, American Bank and Trust Company and Point South, Inc., entered into a loan agreement setting forth the terms and conditions of a construction loan to be made by American Bank and Trust Company to Point South, Inc., and thereafter, also on or about April 13, 1973, Point South, Inc., executed a note and mortgage giving to American Bank and Trust Company a first loan on real property located in Jasper County, South Carolina, known as the reception center site.

Neither said loan agreement nor the note and mortgage executed pursuant thereto contained any restrictions on the assignability by Point South, Inc., or any of its successors-in-title to the property securing said loan, said property hereinabove referred to as the reception center site located on the property at the intersection of U.S. Highway 17 and I-95.

Likewise, the loan agreement, the note and mortgage, none contained any provisions concerning the acceleration of payments due thereunder by Point South, Inc., or terminating advances of funds to be made to Point South, Inc., under the terms of said loan, note and mortgage in the event Point South, Inc., transferred, assigned or otherwise diminished its title-in-interest to the property hereinabove referred to as the reception center site.

7. On or about August 29, 1973, Jeffery Rhodes wrote a letter to Mr. Wade, which read as follows: "Pursuant to our phone conversation enclosed please find the documents for the sale leaseback of the Point South Reception Center. As we discussed, Point South intends to sell the building and assign the mortgage to the purchasing entity. Point South Company and Sea Pines Company will guarantee the financing. We have reserved your first right of refusal to provide the permanent financing. If you have any questions, give us a call. Sincerely, signed Jeffery J. Rhodes."

8. Upon receipt of the said August 29, 1973, letter introduced into evidence as plaintiff's Exhibit No. 2, Mr. Wade made a handwritten note on the bottom which stated as follows: "Shirley — nothing to do but file this." Signed Grady L. Wade, Jr."

9. After the loan agreement and the execution of the note and mortgage, on or about April 13, 1973, American Bank and Trust Company began making disbursements of the loan proceeds to Point South, Inc., as required by the loan agreement, and had disbursed $187,000 of the $250,000 prior to September 7, 1973, September 7, 1973, being the date hereinafter referred to as the execution of the sale and leaseback. On September 7, 1973, Point South, Inc., and Point South Associates executed a sale and leaseback of the property hereinafter described as the reception center site, under the terms of which sale and leaseback Point South, Inc., transferred title or was to transfer title to Point South Associates for a stated consideration, and Point South Associates was to lease the property back to Point South, Inc., for a stated consideration.

10. After September 7, 1973, American Bank and Trust Company continued to advance the loan proceeds of the loan in question to Point South, Inc., until 1974 when the advances were thereafter made directly to Point South Associates, for interest only.

11. On April 13, 1973, Sea Pines Corporation owned ninety percent of the outstanding shares of Point South, Inc., and continental mortgage investors owned ten percent of said shares.

12. Point South, Inc., is a South Carolina corporation. It is a successor to another South Carolina corporation, Twin River Gardens, Inc. Twin River Gardens, Inc., was capitalized in 1964, with $1,000 cash, which satisfied the incorporation statutes of the State of South Carolina in effect at that time.

13. The property located at the intersection of U.S. Highway 17 and I-95, of which the reception center site was a part, was originally acquired by the predecessor corporation of Point South, Inc., Twin River Gardens, Inc., from one Colin Campbell on December 19, 1969. The original acquisition was approximately 1,250 acres and the purchase price therefore was approximately $490,000. The purchase price of the land was partially paid for by Point South, Inc., with its own money, and the balance of the purchase price was paid for with money borrowed by Sea Pines Plantation Company, a South Carolina corporation, and Sea Pines Company, which money was loaned to Point South, Inc., and reflected in the records of Point South, Inc., Sea Pines Company and Sea Pines Plantation Company as inter-company debt.

14. From the date of its inception, Point South, Inc., has adhered to corporate formalities. This includes the

maintenance of regular corporate records, the regular meetings of stockholders, officers, board of directors, and regular election of officers and members of the board of directors, normal and proper accounting procedures and record keeping, and all other corporate formalities which a corporation maintaining its separate identity would perform.

15. During the period of its existence, Point South, Inc., has had as its major stockholder the defendant, Sea Pines Company, at the times in question the defendant owning ninety percent of the outstanding shares in Point South, Inc.

16. During all periods of time in question, the defendant, Sea Pines Company, and Point South, Inc., have had if not identical, certain common directors and officers.

17. During the period of time in question, the subsidiary, Point South, Inc., has been financed in large measure by the parent corporation, Sea Pines Company.

18. At the time that the loan was made by American Bank and Trust Company to Point South, Inc., Point South, Inc., was solvent, having net assets of between $65,000 and $107,000, depending upon which evidence is believed. At that time, in spite of being technically solvent, however, Point South, Inc.'s ratio of liabilities to equity was approximately twenty to one. During the period of time in question, the salaries and other expenses of Point South, Inc., were paid by Sea Pines Company. Probably payment is not the best word to use, though it may be technically correct. The best word may be that these expenses were advanced by the parent company with the expectation and hope that they would be reimbursed by

Point South, Inc. In this instance, because of the financial problems of the Point South, Inc., there was no reimbursement. These funds were paid. It was a normal accounting practice by the parent company with the understanding that they would be repaid at some later date.

19. Though there is no evidence at the time of the loan, on or about April 13, 1973, that Sea Pines Company used the property of Point South, Inc., as its own, there is evidence and to the effect that later it did cause property owned by Point South, Inc., to be mortgaged, and for the loan proceeds which were secured by that mortgage to be applied to the benefit of Sea Pines Company.

20. During the period of time in question, the executives and officers of Point South, Inc., did not act independently of those of Sea Pines Company. We find this primarily because of the identity of such executives and officers, in view of the fact that both companies had approximately the same officers and executives, it seems to us academic that it would be almost impossible for them to act independently, and if they did it would be most difficult for us to ascertain the same.

21. In the last few findings of fact, I have pretty much tracked the *Duplan Corporation against Deering Milliken* case reported in 444 Federal Supplement at page 648, a 1977 Opinion of Judge Hemphill of the District of South Carolina. Particularly referring to page 689, where he lists several factors that may be considered in determining whether or not the corporate veil should be pierced. There are other factors, and of course Judge Russell in the case of DeWitt Truck Brokers, which I'll refer to in some detail

later, lists a number of factors, some of which may not coincide with those that Judge Hemphill has named. But for the purpose of these findings of fact, I have seen fit to track Judge Hemphill. I have stated findings of fact as to the existence of these factors. I do this by way of explanation to shorten what I'm getting ready to say. I would like to now go down these factors and state the knowledge that the plaintiff had of the existence of these factors or the availability of information that should have given the plaintiff knowledge of the existence of these factors.

The plaintiff either knew or should have known of the common stock ownership and the common directors or officers. It is obvious to me that the defendant, Sea Pines Company, made no secret of this. There are numerous exhibits in the record. The one I have before me now is plaintiff's Exhibit 9, dated January, 1973, which is a preliminary prospectus dated December 15, 1972, involving 400 shares of Sea Pines Company common stock. And it's obvious from reviewing this that Sea Pines Company made no secret of the fact of what its relationship with Point South, Inc., was at that time, the pertinent time being on or about April 13, 1973, when the loan was made. That is only one exhibit. There are numerous others, but I find as a fact that prior to the loan, prior to the commitment, the loan being on April 13, 1973, American Bank and Trust Company either knew or in the exercise of due diligence should have known of the common stock ownership and the common directors and officers of Point South, Inc., and Sea Pines Company. Likewise, at these times, American Bank and Trust Company either knew or should have known that the subsidiary, Point South, Inc., was financed to a large extent by the parent. In that regard I refer to defendant's Exhibit 4, which is a letter dated

April 11, 1973, from Point South, Inc., to David G. Gale of American Bank and Trust Company forwarding to the bank a balance sheet of Point South, Inc., dated February 28, 1973, which I assume was being forwarded at the request of the bank to be given consideration in making this loan. And on that statement, it refers to debts due to affiliated companies of $1,671,433. It seems to me that a loan, and there are many other pieces of evidence in the record that should advise the plaintiff of this fact, but that a loan should call to their attention that there was a financing of this corporation by other companies, and they should have either known or they should have found out that this subsidiary was being financed to a large extent by Sea Pines Company.

That document that I referred to also sets forth the figures upon which I made an earlier finding as to the solvency, as to the assets of Point South, Inc., on February 28, 1973, and the ratio of liabilities to capital; that ratio being twenty to one. If there was, in fact, an under-capitalization of this company for the purposes that the company was designed to perform, then at that time American Bank and Trust Company either knew about it or upon the exercises of certainly not even reasonable care but even the slightest degree of care should have known about it.

As to the executives of the subsidiary acting independently of the parent corporation, obviously just a casual examination of the records, just a slight review of what we have in this record and what was made available to the plaintiff or was available for the asking would lead them to conclude that the executives and directors and officers were substantially the same in the two corporations,

and it would be physically impossible for them to act independently of each other.

Now, as to the other items in the Duplan Corporation case, the incorporation of the subsidiary by the parent, obtainment by the parent of the salaries and other expenses or losses of the subsidiary, whether the subsidiary has any substantial business except with the parent and no assets except those conveyed to it by the parent, and the parent using the subsidiary's properties as its own, I don't know of any reason why at the time of the loan American Bank and Trust Company either knew or should have known of the existence of those factors, except to the extent of the debt due to the affiliated companies. The sale and leaseback which was hereinabove referred to dated on or about September 7, 1973, along with a document guaranteeing the lease payments to be made thereunder by Point South, Inc., to its assignee under the sale leaseback, to-wit: Point South Associates, were attached to the aforementioned letter of August 29, 1973, plaintiff's Exhibit 2, which were mailed to Mr. Grady L. Wade of American Bank and Trust Company, by Jeffery Rhodes, financial analyst.

1. Conclusions of law. This court has jurisdiction of this action pursuant to 12 United States Code 1819, and 28 United States Code 1345.

2. The defendant did not guarantee the payment of the April 13, 1973, indebtedness of Point South, Inc., to American Bank and Trust Company. A guarantee is a promise of one to answer for the payment of some debt or the performance of some duty by another, made by another, in case of the failure of that other person who is liable in the first instance to make such payment or performance. The debt or duty may be either present or prospective.

The plaintiff contends that the letter of Sea Pines Company dated August 29, 1973, and offered into evidence as plaintiff's Exhibit 2 evidenced such an agreement on the part of Sea Pines Company to guarantee the loan which had been made by American Bank and Trust Company to Point South, Inc., on or about April 13, 1973, in the amount of $250,000, of which at that point in time $187,000 — approximately $187,000 had been advanced.

The burden is on the plaintiff to establish that such a guarantee was made, and in this case they have failed to carry that burden. The sale and leaseback agreement was attached to that letter. Under the terms of that sale and lease back agreement, Sea Pines Company guaranteed that Point South, Inc., would make those lease payments to Point South Associates. Sea Pines Company contends that the sale and leaseback is a form of financing, and I can well see how it would be. Point South, Inc., transferred the property in question with the encumbrances thereon, with the mortgage of American Bank and Trust Company on the property. Point South Associates bought the property with that encumbrance thereon. The two are tied together, and it seems to me that one could conclude that the payment of the lease payments to Point South Associates would be a way of financing or providing payment for the funds owed to American Bank and Trust Company. I can see how someone would use that word when they said that Sea Pines Company was guaranteeing the financing, and intending to mean that they were guaranteeing the lease payments to be made pursuant to that agreement by Point South, Inc., to Point South Associates.

Appendix C

Oral Order of United States District Court

The testimony in the record is that Mr. Jeffery Rhodes was not an officer of the Sea Pines Company and was not a person authorized to make a guarantee such as this. There is no evidence to the contrary. It seems to me that good business practice would require that an official corporate act be obtained before such a guarantee should be entered into. I see nothing in the corporate records here that any authority was ever obtained. I must assume it was not. These factors raise considerable doubt in my mind what that letter means.

On the other hand, I have the testimony of the plaintiff's witnesses, which say that it meant that they were guaranteeing the financing of the loan already made, much of which already advanced to Point South, Inc.

It's difficult for me to believe that. It's difficult for me to believe that business is handled in that manner, that if that were the understanding, that Mr. Grady Wade would have only written on the bottom of that letter, "Shirley, nothing to do but file this", rather than preparing a formal guarantee agreement, sending it to Sea Pines Company and having it executed. At that point in time, the loan had been made, the note and mortgage had been executed, funds had been advanced. I have serious doubts in my mind as to whether or not any permission — as a matter of fact, my interpretation of the documents is that American Bank and Trust Company could not have prohibited the transfer of the property under the sale lease back, and they would have still had to advance the funds. All of this, when placed into the context of the transaction — or loans secured by a real estate mortgage — compels me to arrive at the conclusion that the plaintiff has failed to establish this guarantee agreement as required in this

case. People normally loan money on real estate mortgages expecting the real estate to be sufficient security, and in this case I'm not convinced that the American Bank and Trust Company did otherwise. So, for the reasons that I have stated, I think that the plaintiff has failed and not by a close margin, but has failed substantially to establish by the greater weight or preponderance of the evidence that this letter of August 29, 1973, and the other actions it relies upon on the part of Sea Pines Company constituted a guarantee by that defendant of the obligation owed to American Bank and Trust Company by Point South, Inc., as evidenced by the note and mortgage executed on or about April 13, 1973.

3. The plaintiff in this case is not entitled to pierce the corporate veil, the corporate veil of the defendant Sea Pines Company and thereby hold that defendant responsible for the obligations of the corporation Point South, Inc., involved in this matter. The defendant, Sea Pines Company, of course, is a ninety percent owner of the stock of Point South, Inc. There is a presumption that the corporation Point South, Inc., and its stockholder, Sea Pines Company, are separate and distinct. The burden rests on the plaintiff to establish a basis for disregarding this normal relationship between stockholder and corporation, or their being separate and distinct, and in this instance, the plaintiff has failed to carry that burden. The case of *DeWitt Truck Brokers, Inc., against W. Ray Flemming Fruit Company,* Fourth Circuit case decided in 1976 and reported in 540 F. 2D 681 is relied upon by me in making this conclusion of law. There is another case on point, a District Court case of this district, decided in 1976, *Duplan Corporation against Deering Milliken, Inc.,* reported in 444 F. Supp. at page 648. That case seems to

indicate that you must consider certain factors, some of which it lists there. If those factors are found to exist, then you pierce the corporate veil. Though I respect all of the judges of the District of South Carolina, my obligation is to follow, when it comes to law, the Fourth Circuit Court of Appeals, unless the United States Supreme Court tells me otherwise, and therefore I'm compelled to disregard the teaching, or what I perceive to be the teaching of the Duplan Corporation case, and to rely on *DeWitt Truck Brokers against W. Ray Flemming Fruit Company,* and that's what I propose to do. I have outlined the factors that should be given consideration, and I have found facts as to those which existed, and I have found facts as to those which the plaintiff either knew or should have known with the exercise of proper care and caution existed, and I see no purpose in reiterating what I have said. Suffice it to say that the plaintiff has established a large number of these factors. But as I read the DeWitt Truck Brokers case, on page 687, the court says that, "In addition to these considerations, there must be present an element of injustice or fundamental unfairness." As Judge Russell said, and I quote: "The conclusion to disregard the corporate entity may not, however, rest on a single factor, whether under capitalization, disregard of corporate formalities or whatnot, but must involve a number of such factors. In addition, it must present an element of injustice or fundamental unfairness."

I see nothing in this case that fits within the category of injustice or fundamental unfairness. There is no intent on the part of the defendant to deceive the plaintiff or, more appropriately, the plaintiff's predecessor, American Bank and Trust Company. All of the facts were made known. All of the facts were made available. There is no

evidence that I can see that the American Bank and Trust Company relied on any of these factors. I think it's more logical to assume and to find that they relied upon the security of their real estate mortgage. I just see nothing in this record that could support a finding of the injustice or fundamental unfairness that Judge Russell speaks of. The plaintiff has referred to a transaction involving a mortgage on Point South, Inc., Real Estate, the proceeds of which or the proceeds of a loan which that mortgage secured went to or was applied for the benefit of the defendant, Sea Pines Company. That may be evidence, and it probably is evidence of the fact that the parent uses the subsidiary's property as its own. But I think that that's all the evidence, and I think that the DeWitt case is clear, that in addition to those factors we must have injustice, fundamental unfairness, and we do not have that in this case.

The order of this court is that the complaint of the plaintiff be and the same is hereby dismissed. Thank you, gentlemen.

Certified:

VINCENT ROLLAND
Official Court Reporter
United States District Court
Florence, South Carolina

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No. 82-1516

In the Supreme Court of the United States

OCTOBER TERM, 1982

SEA PINES COMPANY, PETITIONER

v.

FEDERAL DEPOSIT INSURANCE CORPORATION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

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TABLE OF AUTHORITIES

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FEDERAL DEPOSIT INSURANCE CORPORATION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

Petitioner seeks review of the decision below holding that in the circumstances of this case the district court should have pierced the corporate veil to allow respondent, the Federal Deposit Insurance Corporation, to collect from petitioner the indebtedness owed by its 90%-owned subsidiary.

1. The evidence showed (Pet. App. 1a-5a) that in early 1973 American Bank & Trust ("AB&T") extended a loan to Point South, Inc., a 90%-owned subsidiary of petitioner Sea Pines Company.[1] The purpose of the loan was to finance construction of a reception center on the subsidiary's property. In return AB&T received a $250,000 note

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[1]Point South, Inc. was one of a number of subsidiary corporations used by petitioner. It was initially capitalized with $1,000 by two of the three members of petitioner's executive committee. See Pet. App. 2a. Petitioner and Point South had common directors and officers, and petitioner financed Point South in large part (*id.* at 7a).

secured by a mortgage. In August of that year Point South entered into a sale-leaseback transaction in which it sold the reception center to a limited partnership and leased it back. Petitioner formally guaranteed the rent payable by the subsidiary to the limited partnership.

The following year, in October 1974, petitioner and Point South, acting through their common directors, mortgaged the subsidiary's equity in a 76-acre tract worth $350,000 as collateral for loans to petitioner. Point South was to receive $8,000 as consideration for this transaction. In May 1975 the common directors of petitioner and Point South arranged for cancellation of the 1973 sale-leaseback transaction involving the reception center. Point South repurchased the building and cancelled the note and mortgage issued by the limited partnership. Point South also released petitioner from its agreement to guarantee rent payments on the reception center. During the period in which these latter transactions occurred, Point South was insolvent. In February 1973, Point South's balance sheet showed assets in excess of $2.5 million with a total net worth of $65,000 ($1,000 of capital stock and $64,000 of retained earnings). By February 1974, the highly leveraged subsidiary was insolvent, with a negative net worth of $177,000; by February 1975 the subsidiary had a negative net worth of $1,949,000 (Pet. App. 4a-5a). Point South continued to be insolvent thereafter.

AB&T subsequently failed. The FDIC acquired from the receiver the assets of AB&T, including the $250,000 note and mortgage of Point South. FDIC foreclosed on the mortgage and obtained a deficiency judgment of $196,680.08 against Point South. In October 1978, FDIC sued petitioner to collect the indebtedness owed by Point South, contending that petitioner had guaranteed the debt to AB&T, and, alternatively, that under the circumstances, it was appropriate to pierce the corporate veil to permit recovery from the

parent for the debt of the subsidiary. The district court ruled in favor of petitioner (Pet. App. 14a-29a), concluding that there had been no guarantee of the loan and that, despite the existence of a number of factors that would tend to justify disregard of the separate corporate existence of Point South, the necessary element of fundamental unfairness was lacking.

The court of appeals reversed (Pet. App. 1a-12a). The court of appeals found it unnecessary to determine whether petitioner had guaranteed the loan of its subsidiary, since it concluded that under the circumstances the district court should have pierced the corporate veil to permit recovery against petitioner. The court of appeals noted (*id.* at 7a) that the district court "found that a sufficient number of the factors to pierce the corporate veil were present except the existence of injustice or fundamental unfairness." The court of appeals found such injustice and fundamental unfairness in the fact that the common directors of petitioner and Point South had violated their fiduciary duty to the creditors of the subsidiary by using the subsidiary and its assets for the benefit of the parent during the period in which the subsidiary was insolvent. The court cited the action of the common directors in mortgaging the only unencumbered asset of Point South in order to benefit petitioner, thus depriving the subsidiary of an asset with equity of $350,000, and in cancelling the sale-leaseback transaction, which effectively ended petitioner's guarantee of rent payments that would have been used to continue payments on the AB&T mortgage. The court of appeals concluded that these breaches of fiduciary duty were sufficient to constitute the fundamental unfairness and injustice that, together with factors such as the common officers and directors and the undercapitalization of Point South, would justify piercing the corporate veil.

2. Petitioner contends that the court below overlooked relevant facts, particularly the history of the relationship between petitioner and Point South, and that it used an incorrect legal test that conflicts with an earlier decision of the Fourth Circuit. These contentions are without merit. The court below correctly concluded that petitioner's use of its subsidiary's assets for its own benefit during the period in which the subsidiary was insolvent justified piercing the corporate veil to permit FDIC to recover from petitioner for its subsidiary's indebtedness. That decision, which rests on application of established principles of corporate law, does not conflict with the decision of any other court of appeals or with any decision of this Court. Therefore, review by this Court is not warranted.

Petitioner contends (Pet. 3-6) that this case does not involve the sort of injustice or fundamental unfairness justifying disregard of the corporate entity. But as the court below pointed out (Pet. App. 9a-10a), it is well established that the directors of an insolvent corporation owe a fiduciary duty to creditors of the corporation and may not use the assets of the corporation to prefer themselves. Here the common directors of petitioner and Point South breached that duty by mortgaging the subsidiary's only unencumbered asset in order to benefit petitioner at a time when the subsidiary was insolvent. See *Koehler* v. *Black River Falls Iron Co.*, 67 U.S. (2 Black) 715, 718-721 (1862). Likewise, as petitioner's counsel admitted (see Pet. App. 11a), the cancellation of the sale-leaseback transaction in May 1975 was for the sole benefit of petitioner, with no benefit to the insolvent subsidiary or to creditors such as AB&T. These transactions clearly resulted in the sort of injustice and fundamental unfairness that, together with factors such as the common officers and directors and the undercapitalization of Point South, justifies disregard of the corporate entity under the settled principles of corporate law relied on by the court of appeals.

Petitioner urges that the court of appeals "completely overlook[ed] and ignore[d]" (Pet. 3) the facts before it, in particular that petitioner advanced large sums of money to Point South over a period of time. However, it is clear that the court of appeals did not ignore the facts; the court had the record before it, and its opinion reflects its familiarity with those facts. It was appropriate for the court to examine the period following issuance of the loan by AB&T and during which Point South became insolvent, since that is the period that is relevant to whether there was the injustice to AB&T, and to FDIC as its successor in interest, that would warrant piercing the corporate veil. The fact that petitioner may have been willing to cover the debts of its subsidiary to other creditors and in other periods does not alter the fundamental unfairness and injustice to AB&T and its successor in interest.[2]

Petitioner's contention (Pet. 3) that the decision below "overlooks" and conflicts with *DeWitt Truck Brokers, Inc.* v. *W. Ray Flemming Fruit Co.*, 540 F.2d 681 (4th Cir. 1976), is without merit. The court of appeals referred specifically to the *DeWitt* case and found that the district court had misconstrued it (Pet. App. 9a; *id.* at 7a, 12a). The court in *DeWitt* stated (540 F.2d at 684) that proof of "plain

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[2]The district court made no findings of fact concerning the alleged transfer of funds from petitioner to Point South, but instead relied on AB&T's knowledge of the control petitioner exercised over its subsidiary (Pet. App. 22a-24a).

Petitioner suggests (Pet. 5-6) that FDIC should have been limited to a pro rata recovery of any assets petitioner had received from Point South, since petitioner and one of its affiliates, Sea Pines Plantation Company, were "creditors" by virtue of their transfer of funds to Point South and thus were entitled to participate in Point South assets. Petitioner cites no authority for this suggestion, which appears on its face to be frivolous, and which petitioner apparently advances for the first time in this Court.

fraud" is not necessary in order to disregard the corporate entity, citing this Court's opinion in *Anderson* v. *Abbott*, 321 U.S. 349, 362 (1944). That statement is fully consistent with the conclusion of the court of appeals (Pet. App. 9a, 12a) in this case.[3] Moreover, even if there were a conflict between cases within the Fourth Circuit on this point, this would not be a matter that warrants the attention of this Court. See *Wisniewski* v. *United States*, 353 U.S. 901 (1957).

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[3]Petitioner also suggests (Pet. 3-4) that the decision below conflicts with the decisions of several other courts of appeals that hold that the corporate entity will be disregarded only in exceptional circumstances. There is no such conflict. The cases cited by petitioner are consistent with the conclusion of the court below that the corporate entity may be disregarded even when unfairness or injustice does not take the form of fraud. See *United States* v. *Martin*, 337 F.2d 171, 175 (8th Cir. 1964) (corporate entity will be disregarded when used as an intermediary to "perpetrate fraud or promote injustice"); *In re Gibraltor Amusements, Ltd.*, 291 F.2d 22, 24 (2d Cir.), cert. denied, 368 U.S. 925 (1961) (corporate veil will be pierced when corporate entity is used to defeat public convenience, justify wrong, protect fraud, or defend crime, and in some cases when the subsidiary is used as a mere conduit for the parent); *Chengelis* v. *Cenco Instruments Corp.*, 386 F.Supp. 862, 865 (W.D. Pa.), aff'd mem., 523 F.2d 1050 (3d Cir. 1975) (corporate entity may be disregarded in the case of "fraud or injustice akin to fraud"). See also *Farmers Feed & Supply Co.* v. *United States*, 267 F. Supp. 72, 76 (N.D. Iowa 1967) (corporate veil will not be pierced unless corporation is used as an intermediary to "perpetrate fraud or promote injustice"). While the courts in the cases cited by petitioner declined to pierce the corporate veil, it is significant that none of the cases involved a parent corporation that in effect had stripped the assets of an insolvent subsidiary for its own benefit. Thus, there is no indication that any of these courts would have decided the present case differently than the court below.

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

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General Counsel
Federal Deposit Insurance Corporation

APRIL 1983

DOJ-1983-04